STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE ENROLLED BILL ANALYSIS

Date Amended:	**Enrolled**	Bill No:	**AB 3035**
Tax:	**Property**	Author:	**Huffman**
Related Bills:		Position:	**Support**

BILL SUMMARY

This bill would extend the grace period to qualify for the property tax welfare exemption from 90 days to 180 days on a supplemental assessment.

CURRENT LAW

Property Tax Exemptions. Existing law exempts from property taxation specified types of property or property owned by specified taxpayers. Related to this bill, there are two types of property tax exemptions available to organizations that qualify as exempt organizations under Section 501(c)(3) of the Internal Revenue Code.

- **Church Exemption**. Buildings, land on which they are situated, and equipment used exclusively for religious worship.
- **Welfare Exemption.** Property used exclusively for religious, hospital, scientific, or charitable purposes and owned or held in trust by corporations or other entities that are organized and operating for those purposes, that are nonprofit, and no part of whose net earnings inures to the benefit of any private shareholder or individual.

Supplemental Assessments. Existing property tax law requires property to be reassessed to its current market value whenever there is a change in ownership. "Supplemental assessments" provide a mechanism to immediately reflect the change in assessed value (an increase or decrease) as of the date it occurs for property tax purposes.

Revenue and Taxation Code Section 75.22 provides that a property tax exemption, such as the welfare exemption, will apply to a supplemental assessment triggered by a change in ownership if the person claiming the exemption meets the qualifications for that exemption on that property no later than 90 days after the date of the change in ownership. These provisions also apply to a supplemental assessment triggered by the *completion* of new construction. However, in case of new construction, like constructing a new building, the entire property becomes eligible for the welfare exemption the moment construction *commences* if the intended use of the facilities under construction would qualify the property for the exemption. Because the welfare exemption is generally in effect by the time the new construction is completed, the 90 day grace period to qualify for the welfare exemption in the case of a new construction is generally irrelevant.

PROPOSED LAW

This bill would add Section 75.24 to the Revenue and Taxation Code to provide that notwithstanding Section 75.22, in the case of an organization that qualifies as an exempt organization under Section 501(c)(3) of the Internal Revenue Code that purchases or acquires a property resulting in a "change in ownership" of the property (which results in reassessment of the property to current market value), the property will be eligible for exemption from the supplemental assessment if the organization claiming the exemption is a qualified organization and meets the qualifications for the exemption established by this part no later than 180 days after the date of the change in ownership or the completion of new construction.

IN GENERAL

Supplemental Assessments. Existing property tax law requires property to be reassessed whenever there is a change in ownership or the completion of new construction. A "supplemental assessment" provides a mechanism for picking up a change in assessed value as of the date it occurs. The increase (or decrease) in assessed value is reflected in a prorated assessment (the supplemental assessment) that covers the portion of the fiscal year (July 1-June 30) remaining after the date of change in ownership or completion of new construction. For a change in ownership or completed new construction occurring between January 1 and May 31, two supplemental assessments are issued. The first covers the portion of the current fiscal year remaining after the date of the event; the second covers the ensuing fiscal year in its entirety. An increase in assessed value results in a supplemental tax bill and a decrease in assessed value results in the issuance of a refund check. These supplemental assessments are entered into the "supplemental roll" and contain properties that have changed ownership or had new construction completed, as opposed to the regular "assessment roll" prepared each fiscal year which contains all property in the county.

RELATED LEGISLATION

Sale of Tax Exempt Property – Terminates Exemption. In 2005, SB 555 (Ch. 264 Machado) added Section 75.23 to the Revenue and Taxation Code to immediately terminate a property tax exemption on a property when it is sold if the new property owner is not otherwise eligible for an exemption via the supplemental assessment process. In practical application this means that a person who purchases a property that was previously exempt from property tax, will receive a supplemental assessment that reflects full taxation of the property as of the date of purchase. The increase in assessed value resulting from the change in ownership upon which the supplemental assessment is calculated is the difference of zero (to reflect the prior tax exemption) and the new assessed value of the property. Previously, the new property owner enjoyed a windfall since the property continued to hold the prior owner's tax exempt status for as long as eighteen months, depending upon the date of acquisition.

Construction Activity Starts the Exemption. In recent years, a number of bills have been introduced to modify when a property owned by a nonprofit organization can begin to receive the exemption in the case of vacant land or undeveloped property.

- AB 3074 (AR&T) in 2004 proposed granting the welfare exemption to properties on a retroactive basis for the period between the submission of an application for a building permit and the commencement of actual physical construction.

- AB 783 (Maddox and Mountjoy) in 2003 proposed granting the welfare exemption to properties on the date an application for a building permit was filed. As introduced, it would have started the exemption once various activities such as "seeking" permits, environmental studies, government entitlements and approvals, financing, and contractors.

- AB 2662 (Bogh) in 2002 would have provided that property already in the course of construction will not be considered "abandoned," and therefore no longer eligible for exemption, if construction is delayed due to financing delays or delays in governmental approval.

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by Sonoma County to give nonprofits more time to qualify for the welfare exemption on newly acquired properties.

2. **The income tax exemption does not automatically confer a property tax exemption to a Section 501(c)(3) nonprofit organization.** Property is not eligible to receive the property tax welfare exemption unless it is owned and *operated* by a nonprofit entity for exempt purposes and activities. Under existing law, if a nonprofit organization purchases a property and begins to use the property for an exempt activity within 90 days, it is eligible for exemption from supplemental assessment.

3. **What is a supplemental assessment?** If a property is purchased for $500,000 and its prior assessed value was $200,000, a supplemental assessment in the amount of $300,000 would be processed to reflect the increase in assessed value. If the property purchased is eligible for the welfare exemption, the welfare exemption will be applied to the supplemental assessment and no taxes would ultimately be owed related to the increase in assessed value due to the change in ownership.

4. **It can take longer than 90 days to obtain a special license necessary to operate certain types of properties.** The proposed changes were triggered by a situation in Sonoma County in which a nonprofit organization purchased a residential care facility previously run as a for-profit enterprise. The nonprofit intended to take over the operation of the care facility. However, to do so it needed a license from a governmental agency for the specific location which took longer than 90 days to acquire. To keep the facility in continuous operation it was necessary to lease the facility back to the former owner. Because the property was unable to qualify for the welfare exemption within 90 days of acquiring the property, a supplemental assessment was issued.

5. **In the case of vacant land or undeveloped property owned by a nonprofit organization, a number of bills have been introduced in recent years to modify the point in time when the property can begin to receive the exemption.** This bill would, in some measure, address the issue giving rise to these bills. With this bill, an organization would now have up to 180 days from the date of purchase to begin demolition or construction on property designated for a future exempt use and qualify for a full exemption. Vacant or unused property held for future construction does not qualify for the welfare exemption since it is not being "used" for an exempt purpose and activity. For example, a nonprofit organization may have enough funds to acquire land, but not enough to commence its construction project. Consequently, these properties are subject to property tax.

COST ESTIMATE

The Board would incur insignificant costs (less than $10,000) in informing and advising county assessors, the public, and staff of the change in law and addressing ongoing implementation questions and issues related to this new provision.

REVENUE ESTIMATE

BACKGROUND, METHODOLOGY, AND ASSUMPTIONS

Currently, the welfare exemption will apply to a supplemental assessment triggered by a change in ownership if the purchaser begins exempt activities and qualifies for the exemption no later than 90 days after the date the change in ownership occurred. This provision also applies to supplemental assessments upon the completion of new construction. In the case of new construction, since the welfare exemption is already in effect at the time construction is complete, the effect of the 90 day grace period is generally irrelevant.

Based on a recent survey of county assessors, staff estimates that extending the grace period to qualify for the welfare exemption from 90 days to 180 days will have a minimal revenue impact. Most qualifying organizations make plans to begin the exempt activity once the change in ownership occurs, or immediately thereafter. The same holds true for property upon which that organization begins new construction. The cases in which claims were denied after the 90 day period were rare.

REVENUE SUMMARY

Since so few claims are denied by counties for late filing after the qualifying 90-day grace period, this bill would have a minimal revenue impact.

Analysis prepared by:	Rose Marie Kinnee	(916) 445-6777	7/07/08
Revenue prepared by:	Chris Butler	(916) 445-0840	
Contact:	Margaret S. Shedd	(916) 322-2376	

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